

CHAPTER 11

TAXABILITY OF ANNUITIES

91101. Federal Income Tax

SBP annuities are taxable for federal income tax purposes. A refund of cost resulting from an administrative error, correction of records, or the awarding of DIC is taxable to the annuitant. The member's retired pay tax status has no bearing on the taxability of the annuity or the refund of cost. See table 9---11---1 for exceptions on the taxability of the annuities.

91102. Federal Income Tax Withholding (FITW)

a. General Provisions. SBP annuity payments are income subject to FITW. An annuitant has the right to elect no withholding. In the absence of such an election or if the annuitant does not otherwise submit a withholding certificate, the DFAS Center will withhold on a "married, three exemptions" basis. The annuitant may use TD Form W---4P or any substitute form furnished by the payer.

b. Notice Requirements. The DFAS Center must advise the annuitant of the withholding requirement, and the right to elect no withholding, when making the first payment to the annuitant. Thereafter, the DFAS Center must provide annual notice to the annuitant of the right to elect no withholding, to revoke an election or to submit a new withholding certificate. An annuitant may also submit a withholding certificate at any time to elect no withholding, revoke such election, or request any rate of withholding.

c. One---Time Payments.

(1) **SBP Cost Refunds.** Cost refunds, a "non---periodic distribution," are subject to FITW at the rate of 10 percent unless the annuitant has elected no withholding. The annuitant has the right to make a FITW election on this refund separately from any election already in operation for all other SBP annuity payments.

(2) **Other.** SBP annuity payments, other than the regular monthly entitlement, and other than the cost refunds above, are subject to FITW at the rate of 20 percent unless the annuitant has elected no withholding.

91103. Income Exclusion

In addition to the income exclusion allowed for "consideration for the contract," if the member

retired because of a physical disability resulting from military service and dies after 20 Sep 1972, before reaching normal "retirement age" the survivor may exclude an aggregate of \$5,000 from taxable income on income tax returns. The survivor includes amounts in excess of \$5,000 in gross income. The DFAS Center should, upon request, provide the effective date of cost, the total cost paid (showing separate totals for deductions and direct remittances), the effective date, and amount of annuity.

91104. Adjustment to Taxable Annuity Reserved.**91105. Federal Estate Tax**

The value of the annuity at the time of the member's death may be subject to federal estate tax if any portion of the cost was paid by direct remittance, or if the value of the annuity exceeds the amount that may be excluded from the gross estate. The retired pay activity may furnish the annuitant the current annuity amount and/or a summary of annual payments, and total cost paid (separate totals for deductions and direct remittances). For a computation of the amount of an annuity that will be subject to the tax, if any, the executor of the member's estate may write:

Internal Revenue Service
Chief, Estate and Gift Tax Branch
Attn: CC:IND:E
1111 Constitution Avenue, NW
Wash DC 20224.

91106. State Taxation

Whether SBP annuities are subject to state inheritance or income tax and the method of calculating such tax depend upon the laws of the state concerned. However, the 1099—R information is furnished to the appropriate state tax authority.

91107. Further Tax Information

Survivors should be advised that they may obtain further information concerning taxation or SBP annuities from the local Director of Internal Revenue or the state tax authority.

TABLE 9—11—1				
TAXABILITY OF SURVIVOR BENEFIT PLAN/RETIRED SERVICEMAN'S FAMILY PROTECTION PLAN—NON—RESIDENT ANNUITANTS RESIDING OUTSIDE THE U.S.				
R U L E	A	B	C	D
	If the SBP annuitant resides in the country of	and	then the SBP annuity is	at the rate of
*1	Australia, Belgium, Cyprus, Egypt, Finland, France, Germany, Iceland, Korea, Morocco, Netherlands, Norway, Pakistan, Romania, Trinidad and Tobago, and United Kingdom	is a citizen of the country in which residing	not taxable (note)	
2	Italy	is an Italian national		
3		is not an Italian national	taxable	30 percent.

NOTE: In order to claim entitlement to exemption from taxation based upon a tax convention or treaty, a non—resident alien annuitant is required to file Treasury Form 1001, Ownership, Exemption, or Reduced Rate Certificate, with the appropriate Defense Finance and Accounting Service Center.